Single figure

IS IT POSSIBLE TO MANAGE A COMPANY'S SHORT-TERM LIQUIDITY AS A SINGLE, GLOBAL DAILY POSITION? AT LAST, THE ANSWER CAN BE YES, ACCORDING TO PHILLIP LINDOW AND WILLEM VAN ALPHEN.

The concept of a single, global daily cash position for a company is almost as old as treasury management itself, and has often been cited as the treasurer's nirvana. Today, we believe it is achievable, using the right mix of liquidity management tools, and depending on the structure, culture and functional currencies of the company.

Although there have been few breakthroughs in the management of short-term liquidity since the introduction of the euro back in 1999, there has been a gradual refining of automated liquidity management tools, and of some regulatory environments from both a tax and exchange controls point of view. We now have a situation where the fully automated, multi-currency centre is achievable and can include ever more currencies. For example, it is now possible to set up cross-border sweeps for Polish zloty and Czech koruna, Hong Kong dollars and Singapore dollars, although many other Asian and Latin American currencies still present a challenge to global liquidity structures.

WHY A FULLY AUTOMATED, MULTI-CURRENCY CENTRE? The challenges for today's treasurer are considerable: business has gone global, involving the management of more currencies, countries and entities, in more time zones and regulatory regimes, than ever. At the same time treasury teams are generally leaner, especially at local level; treasury centralisation at regional level has long been the norm. Now companies want to centralise their cash positions on a global basis in order to:

- Know the single global cash position of the company through centralisation of all cash positions;
- Self-fund deficits across the organisation in a timely manner by having access to global surplus working capital; and
- Maximise yield on short-term excess cash and build up core funding positions for increased term investments.

THE STRUCTURE We see a definite trend in the market towards a global view of liquidity management, with techniques originally applied at country level now well used at regional level and moving upscale to create global structures.

The structure illustrated in *Figure 1* shows how funds can be upstreamed on a daily basis, using automated cross-border sweeps, to a designated multi-currency centre. Once there, a single, global cash position can be achieved either by the treasury executing foreign exchange (FX) swaps in the market, or through the use of a cross-currency notional pool.

There are distinct advantages to using a cross-currency notional pool. Since funds remain in separate accounts and in the name of the relevant subsidiaries, no intercompany transfers are created, reducing administration requirements. Notional pooling also optimises interest earnings in a fully automated way, leaving treasury staff free for other cash and treasury management activities.

But a cross-currency notional pool will not always be achievable, and in other cases, the treasurer may prefer to execute FX swaps. To understand how a multi-currency centre can be achieved, let's have a look at today's advanced toolkit for liquidity management.

THE TOOLKIT Not all the tools are available from all banks, but they are generic and fairly widely available. Obviously, a bank with a wide geographic footprint will be able to meet the needs of more companies in more markets.

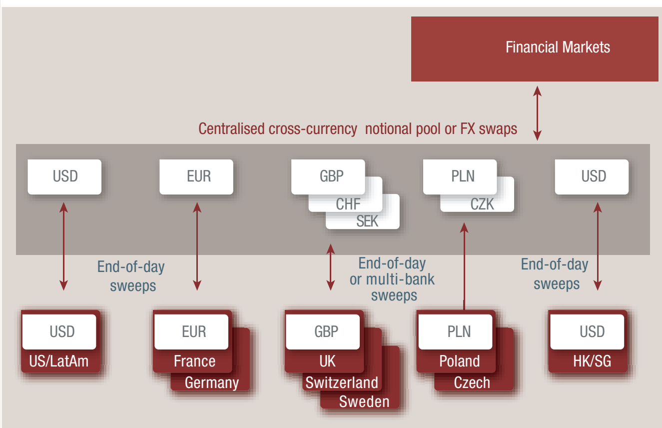
End-of-day sweeping (cash concentration) Typically, this tool will be used to sweep funds from local accounts with a cash management bank to central treasury control. This allows local treasury or finance staff to manage intra-day positions, with end-of-day positions consolidated to the multi-currency centre. End-of-day sweeping arrangements must fit well with a company's regional activities, give same-day value, and should also offer a flexible range of set-up possibilities, including trigger, target and constant balancing.

Multi-bank cash concentration This tool automates the collection of funds from accounts with third-party banks to an account held with the cash management bank. It uses Swift MT940 and MT942 messages to maintain balance information at the bank's central pooling engine, generating request for transfer messages to trigger fund concentration. This tool comes into play when a company needs to maintain accounts outside its cash management bank's footprint – for example, to facilitate local payroll – but still wishes to centralise funds. As with end-of-day sweeping, multi-bank cash concentration should offer flexible specification parameters for time and frequency of transfers, minimum/maximum sweep amounts and target residual balances left on the local accounts.

Executive summary

- How a fully automated, multi-currency centre can be set up using the right combination of liquidity management tools available in the market today. It's all about mastering the art of the possible.

Figure 1. Goal: global multi-currency centre



Global end-of-day sweeping for dollars and euros Where companies need to convert local currency positions to US dollars or euros as functional currencies, automated end-of-day sweeps allow dollars and euro cash positions to integrate into centralised treasury positions as if they were local accounts, with same-day value and book date of sweep day +1. End-of-day "follow the sun" sweeping for dollars and euros is a key enabler of the automated, multi-currency centre.

Cross-currency notional pooling Some company structures may also allow a single-currency notional pool to be effective.

Notional pooling allows for interest offset on concentrated balances by offsetting the debit and credit balances across multiple accounts (and multiple currencies) to achieve an interest margin over compensated balances. This is achieved without co-mingling funds or requiring physical FX swaps, and interest returns are automatically re-applied to the accounts (in compliance with regulatory and fiscal requirements).

Reporting tools Typically, reporting will be via the usual electronic banking routes or via email. If sweeping is used to concentrate funds into a single account in treasury ownership, intercompany loans will be created, which must be tracked and recorded. An automated tracking tool provides the necessary reporting of these transactions and of the resulting intercompany loan positions.

The impact of SEPA on liquidity management The benefits of the Single Euro Payments Area (SEPA) will be felt particularly in the area of payments, where it will no longer be necessary to maintain disbursement accounts in each country, although it will take much longer to fully centralise collections, given the persistence of cheques and local collection instruments. What is clear, though, is that SEPA will in time offer a further opportunity for refining and fine-tuning liquidity management capabilities.

THE ART OF THE POSSIBLE Creating a fully automated, multi-currency treasury centre is all about mastering the art of the possible. When, where and how will a multi-currency treasury centre model be effective? The account structure for a multi-currency centre will usually be held in Europe, probably in London or Amsterdam. But this does not necessarily mean it is only achievable for European headquartered companies. Research has found that while 59% of companies centralise all their dollar accounts in the US, 42% of US companies and 69% of European companies centralise their offshore dollar in Europe.

Companies in dollar-driven industries such as oil, shipping and transportation, were the first to move towards multi-currency centres for global liquidity management. Now multinational manufacturers are considering the possibilities for bringing more liquidity, and more currencies, into one centre. For example, we have implemented a cash consolidation and pooling structure encompassing 44 legal entities, 97 accounts and six currencies across North America, Europe and Asia for one company.

Middle-market companies can also benefit, not least because a cross-border sweeping and cross-currency notional pooling arrangement is an efficient liquidity management tool for lean treasury teams. Over recent months, several such companies have adopted such structures.

Of course, companies with funding requirements (as opposed to the cash-rich) are most likely to put thought and effort into maximising their short-term liquidity. Creating an automated, multi-currency centre is just one way to use the flexible and comprehensive liquidity toolkit available today. And as the tools and the regulatory environments continue to evolve, we see a single global cash position as more and more achievable.

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